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The Dormant Commerce Clause and State-Mandated Preference Laws in Public Contracting: Developing a More Substantive Application of the Market-Participant Exception

Benjamin C. Bair

INTRODUCTION

You are a state legislator. Your state's highway construction industry has seen better days, and unemployment is rising. Nevertheless, cities and counties in your state are hiring nonresident construction workers and buying cement and gravel from nonresident suppliers. Your constituents are upset that their tax dollars are going to outsiders, so you decide to draft a bill requiring all local governments¹ in your state to fill at least half of their highway construction positions with state residents. Is such a law valid under the Commerce Clause² of the United States Constitution?

The Supreme Court has interpreted the Commerce Clause as restricting the states' power to regulate interstate commerce, even when Congress has chosen not to regulate in a particular area.³ More specifically, the Court has construed the Commerce Clause to proscribe states from discriminating economically against other states or from adopting regulatory legislation that burdens interstate commerce to a substantially greater extent than it provides local benefits.⁴ Because this restriction results from the Commerce Clause's unstated "negative" implications rather than its explicit command, it falls under the rubric of the "dormant Commerce

1. "Local governments" include city governments, county governments, municipal governments, school boards, or the governing bodies of any other political subdivisions of the state.

2. The Commerce Clause states that Congress shall have the power to "regulate Commerce . . . among the several states." U.S. CONST. art. I, § 8, cl. 3.

3. *See, e.g., Oklahoma Tax Comm'n. v. Jefferson Lines, Inc.*, 115 S. Ct. 1331, 1335 (1995) (explaining that the Supreme Court has historically interpreted the Commerce Clause as limiting state regulatory power); *New Energy Co. v. Limbach*, 486 U.S. 269, 273 (1988) ("It has long been accepted that the Commerce Clause not only grants Congress the authority to regulate commerce among the states, but also directly limits the ability of the states to discriminate against interstate commerce."); *see also Case of the Freight Tax*, 82 U.S. (15 Wall.) 232 (1873) (adopting this interpretation of the Commerce Clause for the first time).

4. *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970), states:
Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is clearly excessive in relation to the putative local benefits. If a legitimate local purpose be found, then the question becomes one of degree.
397 U.S. at 142 (citation omitted).

Clause.”⁵ By interpreting “these great silences of the Constitution,”⁶ the Supreme Court has used the dormant Commerce Clause to strike down state laws that discriminate against nonresidents or that unduly burden interstate commerce.⁷

The Supreme Court has created an exception to the dormant Commerce Clause, however, that grants states some power to discriminate economically against nonresidents in favor of residents. This “market-participant” exception allows a state freely to adopt contracting preferences towards residents if the state participates in the market as the buying, hiring, or selling agent.⁸ Under this exception, the Supreme Court has upheld state laws favoring residents when a state purchases scrap metal,⁹ buys printing services,¹⁰ sells cement,¹¹ or hires construction workers.¹² Local governments can also adopt laws preferring residents for such public contracts.¹³

It remains unclear under the dormant Commerce Clause whether a state government may adopt a “state-mandated preference law” — a law requiring local governments within the state to prefer state residents for public contracts.¹⁴ Many states have en-

5. *New Energy Co.*, 486 U.S. at 273-74; LAURENCE H. TRIBE, *AMERICAN CONSTITUTIONAL LAW* § 6-2, at 403 (2d ed. 1988).

6. *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 535 (1949).

7. See, e.g., *Philadelphia v. New Jersey*, 437 U.S. 617 (1978) (holding unconstitutional a New Jersey statute that prohibited the importation of solid or liquid waste originated or collected outside the state); *Dean Milk Co. v. Madison*, 340 U.S. 349 (1951) (holding unconstitutional a Madison, Wisconsin ordinance that prohibited the sale of milk unless bottled within five miles of the city); *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511 (1935) (holding unconstitutional a New York statute that set a minimum price for milk sold in the state by nonresident producers).

8. See *Reeves, Inc. v. Stake*, 447 U.S. 429, 436 (1980) (distinguishing between “States as market-participants and States as market regulators”).

9. See *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976).

10. See *American Yearbook Co. v. Askew*, 339 F. Supp. 719 (M.D. Fla.), *aff'd*, 409 U.S. 904 (1973).

11. See *Reeves*, 447 U.S. at 446-47.

12. See *White v. Massachusetts Council of Constr. Employers, Inc.*, 460 U.S. 204 (1983).

13. See *White*, 460 U.S. at 214-15 (holding that a city spending its own money on public contracts may have hiring preferences for city residents because it is a market participant).

14. “Public contracts” include hiring for public construction jobs, purchasing goods with public funds, or selling goods made from public funds. “Preferring” residents or adopting “in-state preferences” means giving residents some advantage in obtaining public contracts.

The hiring preference statute involved in *W.C.M. Window Co. v. Bernardi*, 730 F.2d 486 (7th Cir. 1984), provides a useful example of a state-mandated preference law. The statute in that case stated that the contractor on “any public works project or improvement for the State of Illinois or any political subdivision . . . thereof shall employ only Illinois laborers on such project or improvement,” unless the contractor certifies . . . that Illinois laborers either “are not available, or are incapable of performing the particular type of work involved.” 730 F.2d at 489 (quoting ILL. REV. STAT. ch. 48, § 271 (1981)). Violation of the preference law was a misdemeanor punishable by a maximum jail sentence of 30 days and a maximum fine of \$500. 730 F.2d at 489 (citing ILL. REV. STAT. ch. 48, § 274; ch. 38, §§ 1005-8-3(a)(3), 1005-9-1(a)(3) (1981)).

This Note only examines the *federal* constitutionality of state-mandated preference laws. State constitutional or legislative limitations, particularly self-government and home-rule pro-

acted such preference laws,¹⁵ but the federal circuit courts of appeals are split as to whether the Constitution permits them. The Seventh Circuit struck down a state-mandated preference law under the dormant Commerce Clause.¹⁶ In contrast, the Ninth and Third Circuits upheld state-mandated preference laws as constitutional under the dormant Commerce Clause.¹⁷ The dispute between the circuits centers on the characterization of the relationship between the state and local governments within the state. The Ninth and Third Circuits followed the traditional view that local governments are merely dependent political subdivisions.¹⁸ Thus, they held that the state acts as a market-participant when it enacts a state-mandated preference law.¹⁹ The Seventh Circuit repudiated this traditional view and decided that the local government in the case before it possessed substantial autonomy from the state government. Thus, it held that the state acts as a market regulator, which is unconstitutional under the dormant Commerce Clause,

visions, may restrict the adoption of such laws. See, e.g., *Novak v. Perk*, 413 N.E.2d 784, 786 (Ohio 1980) (stating that "municipal exercises of authority which involve powers of local self-government ordinarily prevail over general state laws"); *Portland v. Welch*, 59 P.2d 228, 231 (Or. 1936) (stating that "[t]he object and purpose of such constitutional provision is to prevent legislative interference and intermeddling with purely municipal affairs"); see also 1 CHESTER J. ANTIEAU ET AL., *MUNICIPAL CORPORATION LAW* § 3.01, at 7 (1995) ("Home rule is important to cities in two principal ways. First as a source of municipal power. Secondly, as a limitation upon legislative control."); cf. *Associated Gen. Contractors v. San Francisco*, 813 F.2d 922 (9th Cir. 1987) (holding that the city charter partially invalidated a city ordinance preferring locally-owned businesses in city contracting).

15. See, e.g., ALASKA STAT. § 36.15.050(a) (1994); CAL. GOVT. CODE § 4331 (West 1966); ILL. REV. STAT. ch. 48, ¶¶ 269-74 (1981); KAN. STAT. § 75-3740 (1969).

Risk averse states can take the path chosen by Ohio. Instead of mandating preferences on local governments, Ohio developed a model system of preferences that any local government may voluntarily adopt. See OHIO ADMIN. CODE 123:5-1-32 (1994) (adopted pursuant to OHIO REV. CODE ANN. § 125.111 (Anderson 1994)). Ohio based the model preference on a state-level preference law already in existence. OHIO REV. CODE ANN. §§ 125.09, 125.111 (Anderson 1994). This path may not achieve all of the beneficial effects sought by the state, but it would be constitutionally permissible because cities are currently free to adopt their own preferences. *White*, 460 U.S. at 204.

16. See *W.C.M. Window Co. v. Bernardi*, 730 F.2d 486, 496-98 (7th Cir. 1984).

17. See *Big Country Foods, Inc. v. Board of Educ.*, 952 F.2d 1173 (9th Cir. 1992); *Trojan Technologies, Inc. v. Pennsylvania*, 916 F.2d 903 (3d Cir. 1990), cert. denied, 501 U.S. 1212 (1991). The statute in *Trojan Technologies* was actually a buy-American law rather than a state resident preference, but this fact did not alter the court's analysis of the market-participant issue. See 916 F.2d at 909-12. This fact does matter, however, under the test this Note proposes. See *infra* notes 125-28 and accompanying text.

18. See, e.g., *United Bldg. & Constr. Trades Council v. Mayor of Camden*, 465 U.S. 208, 215 (1984); *Trenton v. New Jersey*, 262 U.S. 182, 187 (1923) (stating that a state "may withhold, grant or withdraw powers and privileges as it sees fit. However great or small [the municipality's] sphere of action, it remains the creature of the State exercising and holding powers and privileges subject to the sovereign will."); see also 1 ANTIEAU, *supra* note 14, § 2.00 (discussing the nearly complete control by states of municipalities); *infra* notes 45-46 and accompanying text.

19. See *Big Country*, 952 F.2d at 1179; *Trojan Technologies*, 916 F.2d at 911-12.

when it adopts a state-mandated preference law, at least when that law applies to an autonomous local government.²⁰

This Note argues that the current focus on the relationship between states and their local governments as the key determinant of the constitutional validity of state-mandated preference laws is flawed. Instead, a court considering the validity of a state-mandated preference law should uphold such a law only if it distributes the benefits of state expenditures to state residents and does not excessively burden interstate commerce.

Part I describes dormant Commerce Clause doctrine and the market-participant exception. This Part then argues that courts currently evaluate whether to apply the market-participant exception to state-mandated preference laws based on whether they characterize the local governments affected by the law as politically dependent subdivisions of the state or as autonomous entities. Part II examines the theoretical rationales for the market-participant exception and argues that the moral and political entitlement of state residents to state funds, and the built-in spending restraints of resident-preference laws, are the rationales that actually justify the market-participant exception and define its scope. This Part then applies these rationales to state-mandated preference laws and argues that courts should uphold some of these laws under the market-participant exception. This Part also explains why the current focus on state-local government relationships fails to identify those state-mandated preference laws that are supported by the rationales for the market-participant exception. Part III draws on dormant Commerce Clause and Privilege and Immunities Clause²¹ jurisprudence and concludes that under the market-participant exception to the dormant Commerce Clause, a court should permit a particular state-mandated preference law if the state is spending the funds of its own residents, if no nondiscriminatory alternatives exist, and if the law's burden on interstate commerce does not substantially outweigh its local benefit.

I. THE DORMANT COMMERCE CLAUSE, THE MARKET-PARTICIPANT EXCEPTION, AND THE CURRENT APPROACH TO STATE-MANDATED PREFERENCE LAWS

Because state-mandated preference laws interfere with interstate commerce and discriminate economically against nonresidents, such laws may violate the dormant Commerce Clause. If

20. See *W.C.M. Window*, 730 F.2d at 495.

21. The Privileges and Immunities Clause states that "[t]he Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States." U.S. CONST. art. IV, § 2.

state-mandated preferences are to pass constitutional muster under current law, they must fall within the market-participant exception to the dormant Commerce Clause. Section I.A summarizes dormant Commerce Clause jurisprudence. Section I.B then describes the market-participant exception to the dormant Commerce Clause. Finally, section I.C argues that courts currently evaluate whether to apply the market-participant exception to state-mandated preference laws based on how they characterize the relationship between the state and the local governments within the state.

A. *The Dormant Commerce Clause*

The dormant Commerce Clause prohibits state regulations that unnecessarily burden interstate commerce. Its main thrust is to preserve the national economy and to prevent the political and economic balkanization of the states that occurred under the Articles of Confederation, when states fought destructive trade wars with each other.²² Although Commerce Clause doctrine has varied considerably over time,²³ the current test for state regulations under the dormant Commerce Clause focuses on two distinct elements.

First, the state must be pursuing a legitimate state end.²⁴ The Court generally has accepted health, safety, and welfare concerns as legitimate state ends,²⁵ but it usually rejects economic concerns, particularly when the state economically discriminates in favor of

22. See, e.g., *Oklahoma Tax Commn. v. Jefferson Lines, Inc.* 115 S. Ct. 1331, 1335-36 (1995) (stating that "the Commerce Clause's purpose [is] preventing a State from retreating into economic isolation or jeopardizing the welfare of the Nation as a whole" and citing numerous historical references relating to the prevention of economic balkanization that occurred under the Articles of Confederation); *H.P. Hood & Sons v. DuMond*, 336 U.S. 525, 533-35 (stating that the Framers designed the Commerce Clause to protect "the peace and safety of the Union" and to promote "solidarity and prosperity"); see also Letter of February 13, 1829, from James Madison to J.C. Cabell, in 3 *THE RECORDS OF THE FEDERAL CONVENTION OF 1787*, at 478 (M. Farrand ed., 1911) (stating that the Commerce Clause "grew out of the abuse of the power by the importing States in taxing the non-importing, and was intended as a negative and preventive provision against injustice among the States themselves").

23. Initially, the Supreme Court attempted to distinguish between "local" regulations pursuant to the state's police power and "national" regulations that required uniform treatment. See *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299 (1851). Later, the Court attempted to distinguish between regulations that "directly" or "indirectly" affected interstate commerce. See, e.g., *Seaboard Air Line Ry. v. Blackwell*, 244 U.S. 310 (1917); *Smith v. Alabama*, 124 U.S. 465, 482 (1888). The Court eventually abandoned this approach in *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937), and *Wickard v. Filburn*, 317 U.S. 111 (1942), for more empirically based tests. See *TRIBE*, *supra* note 5, § 5-4. For the current test under the dormant Commerce Clause, see *infra* notes 24-32 and accompanying text.

24. See *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

25. See, e.g., *Maine v. Taylor*, 477 U.S. 131 (1986) (recognizing that protecting the state's baitfish population was a legitimate objective); *Mintz v. Baldwin*, 289 U.S. 346 (1933) (holding that states may require nonresident suppliers of cattle to certify that the cattle are free of Bang's disease).

residents over nonresidents.²⁶ One of the primary motivations for protecting nonresidents from such discriminatory measures is that they are not represented in the political process of the discriminating state. Therefore, they have no way of protecting themselves from the adverse economic effects of other states' regulations.²⁷ The Court has upheld even facially discriminatory statutes, however, when the proffered justifications were sufficiently important.²⁸

If a court determines that the state is pursuing a legitimate state end, then it will measure whether the burden of the regulation on interstate commerce substantially outweighs the putative local benefit.²⁹ In performing this analysis, the court may look to whether the state could have adopted any less discriminatory or less burden-

26. See *Lewis v. BT Investment Mgrs., Inc.*, 447 U.S. 27 (1980) (holding unconstitutional a statute that prevented nonresident banks and bank holding companies from owning a resident investment advisory firm); *Hunt v. Washington State Apple Advertising Commn.*, 432 U.S. 333 (1977) (holding unconstitutional a statute that required nonresident producers of apples to repack their product or change their labeling); see also *C & A Carbone, Inc. v. Town of Clarkston*, 114 S. Ct. 1677, 1683 (1994) (stating that "[d]iscrimination against interstate commerce in favor of local business or investment is *per se* invalid, save in a narrow class of cases in which the municipality can demonstrate, under rigorous scrutiny, that it has no other means to advance a legitimate local interest"); *City of Philadelphia v. New Jersey*, 437 U.S. 617, 624 (1978) (stating that "simple economic protectionism" is subject to a virtually *per se* rule of invalidity).

27. See *Kassel v. Consolidated Freightways Corp.*, 450 U.S. 662, 675 (1981) (rejecting the presumption that "a State's own political processes will serve as a check against unduly burdensome regulations" when those regulations discriminate against interstate commerce); *Southern Pac. Co. v. Arizona*, 325 U.S. 761, 767-68 n.2 (1945) ("[T]he Court has often recognized that to the extent . . . the burden of state regulation falls on interests outside the state, it is unlikely to be alleviated by the operation of those political restraints normally exerted when interests within the state are affected."); see also *TRIBE*, *supra* note 5:

In [the dormant Commerce Clause] context, the rhetoric of judicial deference to democratically fashioned judgments of legislatures is often inapposite. The checks on which we rely to curb the abuse of legislative power — election and recall — are simply unavailable to those who have no effective voice or vote in the jurisdiction which harms them. . . . Whatever may be the general merit of a system of judicial review which sanctions intervention by the counter-democratic courts only when the normal processes of democracy have broken down, that model is of little use if mechanically applied in the context of interstate commerce, where problems often arise precisely because the individual state's democratic processes have worked well.

Id. § 6-5, at 409 (citation omitted).

28. See *Maine v. Taylor*, 477 U.S. 131 (1986) (upholding a ban on the importation of live baitfish infected with parasites).

29. See *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970). Some members of the Court disfavor balancing in the dormant Commerce Clause context. See *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 95 (1987) (Scalia, J., concurring) (stating that the balancing test is "ill suited to the judicial function and should be undertaken rarely if at all"); *Kassel*, 450 U.S. at 691-92 (Rehnquist, J., dissenting) (arguing that the balancing test could lead to anomalous results in similar cases); see also Donald H. Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091, 1101-08, 1197 (1986) (arguing that the Court, despite its language, actually has not performed any balancing and should not do so except in the context of the market-participant exception). The *Pike* test remains the law, however. See *C & A Carbone, Inc. v. Town of Clarkston*, 114 S. Ct. 1677, 1682 (1994).

some alternatives.³⁰ On the one hand, if the state cannot present sufficient evidence that the regulation provides a substantial and legitimate local benefit, especially if the statute discriminates against nonresidents, then the court will usually strike down the statute as a violation of the dormant Commerce Clause.³¹ On the other hand, if the state can present evidence that the statute presents only a small burden, particularly when that burden applies to both residents and nonresidents equally, then the court will probably uphold the law.³²

B. *The Market-Participant Exception to the Dormant Commerce Clause*

Under the market-participant exception to the dormant Commerce Clause, a state may burden commerce or even facially discriminate against nonresidents whenever it engages in "direct . . . participation in the market."³³ The Supreme Court created the exception in *Hughes v. Alexandria Scrap Corp.*,³⁴ in which it upheld a

30. See, e.g., *Hughes v. Oklahoma*, 441 U.S. 322 (1979) (holding that while the state could legitimately protect its minnow supply, it had not tried to do so in a nondiscriminatory fashion); *A & P Tea Co. v. Cottrell*, 424 U.S. 366 (1976) (holding that if other states refuse to accept Mississippi milk, Mississippi's remedy should be a court challenge rather than exclusion of the discriminatory state's milk); *Dean Milk Co. v. Madison*, 340 U.S. 349, 354-56 (1951) (stating that the state could have protected residents from tainted milk without completely prohibiting the importation of milk into the city).

31. See, e.g., *Kassel*, 450 U.S. at 662 (holding unconstitutional a prohibition on the use of trucks longer than 65 feet because it disproportionately affected nonresidents); *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978) (holding unconstitutional a regulation that prohibited the importation of solid waste from nonresidents); *Southern Pac. Co. v. Arizona*, 325 U.S. 761 (1945) (holding unconstitutional a prohibition on the use of longer trains than common in Arizona because the improvement in safety was marginal compared to the restriction on interstate commerce).

32. See, e.g., *South Carolina State Highway Dept. v. Barnwell Bros.*, 303 U.S. 177 (1938) (holding constitutional a prohibition on the use of particularly heavy trucks because the regulation affected both intrastate and interstate traffic). But see *Bibb v. Navajo Freight Lines*, 359 U.S. 520 (1959) (holding unconstitutional a nondiscriminatory regulation requiring certain mudguards because the safety advantages were unclear).

Technically, courts have examined a third element: whether the proposed regulation is rationally related to the state's legitimate objective. See *Barnwell Bros.*, 303 U.S. at 191-92. Practically, however, this requirement is empty. The Court has expressed its willingness to defer to legislative decisions for this requirement. See *Barnwell Bros.*, 303 U.S. at 189-92. Moreover, the examination of less discriminatory alternatives will ensure that the regulation not only rationally relates to the state's objective but also that it achieves that objective better than other regulations.

33. *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204, 208 (1983) (quoting *Reeves, Inc. v. Stake*, 447 U.S. 429, 436 n.7 (1980) (Powell, J., dissenting)).

34. 426 U.S. 794 (1976). Arguably, *American Yearbook Co. v. Askew*, 409 U.S. 904 (1972), was the first case in which the Court recognized a distinction between state regulation and state market activity. In *Askew*, a panel of three district court judges upheld under the Commerce Clause a Florida statute requiring all public printing for the state to be done within the state. 339 F. Supp. 719, 725 (M.D. Fla. 1972). The Supreme Court merely affirmed the opinion of the panel, however, without explaining its specific reasoning. 409 U.S. at 904.

Maryland statute that promised a cash "bounty" to scrap processors licensed by the state for the destruction of any vehicle formerly titled in Maryland. The Court held that when the state eschews its role as a government entity and enters the market as a "private actor," as Maryland did when it offered to buy the vehicles, then the dormant Commerce Clause does not govern its activities.³⁵ Under this market-participant exception, the Court has also upheld a state's ability to sell state-produced cement preferentially to residents³⁶ and to hire residents over nonresidents for public construction projects.³⁷

The Court has created two notable limitations on the applicability of the market-participant exception. In *South-Central Timber Development v. Wunnicke*,³⁸ Alaska adopted a requirement that all successful bidders on state-owned timber resources partially process the timber in Alaska prior to shipping it out of the state.³⁹ The Supreme Court held that this "primary manufacture" requirement violated the dormant Commerce Clause because the state was attempting to control the post-contractual disposition of the timber. The Court explained that this "downstream restriction" made the market-participant exception inapplicable because the state was attempting to govern separate, private economic relationships.⁴⁰ In *New Energy Co. v. Limbach*,⁴¹ an Ohio statute provided a tax credit for sales of Ohio-produced ethanol. It did not provide that credit for ethanol produced in another state, however, unless that state had a reciprocal tax credit for Ohio-produced ethanol.⁴² The Supreme Court struck down the statute, stating that taxation is a "primeval government activity" that is not analogous to private market activity.⁴³ Thus, the market-participant exception generally will not apply to any state activity that comes closer to traditional government functions like regulation or taxation, although it is far from clear how courts should make this distinction in specific cases.

C. *State-Mandated Preference Laws and the Market-Participant Exception*

Courts applying the market-participant test to state-mandated preference laws have focused on the relationship between the state

35. *Alexandria Scrap*, 426 U.S. at 805-10.

36. *See Reeves*, 447 U.S. at 429.

37. *See White*, 460 U.S. at 214-15.

38. 467 U.S. 82 (1984).

39. *See* 467 U.S. at 84-86.

40. 467 U.S. at 98-99.

41. 486 U.S. 269 (1988).

42. *See* 486 U.S. at 271-73.

43. 486 U.S. at 277.

passing such a law and its local governments to determine the applicability of the exception. Because the market-participant exception focuses on whether the state is "directly participating" in the market or whether it is "regulating" the market,⁴⁴ courts have attempted to decide whether states are acting *through* their local governments as political agents or whether they are acting *on* their local governments' distinct contracting activity. There are essentially two different views of this relationship that courts have taken — the traditional view of local governments as "creatures of the state" and the more contemporary view of local governments as potentially autonomous entities.

Under traditional doctrine governing state-local relationships, states enacting state-mandated preference laws would always be acting as market-participants. Traditionally, courts viewed local governments as dependent "political subdivisions" or "creatures of the state."⁴⁵ Applying this doctrine, a state enacting a state-mandated preference law would merely be restricting the contracting activity of one of its own political arms. All contracts with the local government essentially would be contracts with the state. Therefore, under this interpretation, states enacting state-mandated preference laws would be "directly participating" in the market.⁴⁶

Under a more contemporary — and more complex — interpretation of state-local relationships, states enacting state-mandated preference laws would be market participants only in certain circumstances. The Supreme Court often has treated local governments as distinct, separate entities from state governments. For example, local governments do not share state immunity from anti-trust laws⁴⁷ or section 1983 constitutional tort actions.⁴⁸ In addition, the Eleventh Amendment does not bar suits against local governments in federal court,⁴⁹ and local governments are citizens for purposes of diversity jurisdiction.⁵⁰ For the purpose of deter-

44. See *supra* notes 34-43 and accompanying text.

45. See, e.g., *Williams v. Mayor of Baltimore*, 289 U.S. 36, 40 (1933); *City of Trenton v. New Jersey*, 262 U.S. 182, 188 (1923); see also 1 ANTIEAU, *supra* note 14, § 2.00 (stressing that states have nearly complete control of local governments). See generally Carol F. Lee, *The Federal Courts and the Status of Municipalities: A Conceptual Challenge*, 62 B.U. L. Rev. 1 (1982).

46. See, e.g., *Big Country Foods v. Board of Educ.*, 952 F.2d 1173, 1179 (9th Cir. 1992); *Trojan Technologies v. Pennsylvania*, 916 F.2d 903, 911 (3d Cir. 1990), *cert. denied*, 501 U.S. 1212 (1991).

47. See *Community Communications Co. v. City of Boulder*, 455 U.S. 40 (1982).

48. See *Monell v. Department of Soc. Serv.*, 436 U.S. 658 (1978).

49. See *Mt. Healthy City School Dist. Bd. of Educ. v. Doyle*, 429 U.S. 274, 280-81 (1977); *Workman v. New York*, 179 U.S. 552, 563-66 (1900).

50. See *Moor v. Alameda County*, 411 U.S. 693 (1973).

Treating local governments as independent entities also comports more with legal and political reality. State constitutions often confer significant spheres of power to local governments through home-rule provisions. See *supra* note 14. Although home-rule provisions

mining the applicability of the market-participant exception to states enacting state-mandated preference laws, courts could evaluate the autonomy of the particular local government entity affected by the law.⁵¹ If the local government is actually dependent, then the result should be the same as under traditional doctrine — the state is acting as a market participant. But, if the local government possesses substantial independence — through its ability to raise revenues or control its own affairs, for example — then the state would be regulating the economic activity of an independent actor and would not be a market participant.⁵²

Therefore, courts applying either the traditional or the more contemporary approach to state-local government relationships must focus on the dependence of the local government as the key to applying the market-participant exception to state-mandated preference laws. Courts applying the traditional approach assume dependence, while courts applying the more contemporary approach actually measure dependence. Under both approaches, states mandating preferences on *dependent* local governments are acting as market participants, whereas states mandating preferences on *autonomous* local governments are acting as regulators.

There are two potential problems with treating state and local governments as a single market participant. One problem is that state governments often do not have formal privity of contract with local construction workers, which makes a state-mandated preference law look more like regulation than direct market-participation. *White v. Council of Construction Employers*,⁵³ however, suggests that formal privity is not necessary. In *White*, the mayor of Boston had issued an executive order requiring that all construction projects funded by the city have a work force composed of at least fifty percent Boston residents.⁵⁴ The Council argued that the

have not always been successful in guaranteeing local autonomy, *see, e.g.*, Gerald Frug, *The City as a Legal Concept*, 93 HARV. L. REV. 1057, 1117 (1980); Terrance Sandalow, *The Limits of Municipal Power Under Home Rule*, 48 MINN. L. REV. 643, 652 (1964), such provisions have generally given local governments considerable lawmaking power. *See* Richard Briffault, *Our Localism: Part I — The Structure of Local Government Law*, 90 COLUM. L. REV. 1, 9-18 (1990) (defending the effectiveness of home-rule provisions).

51. *See, e.g.*, *W.C.M. Window Co. v. Bernardi*, 730 F.2d 486, 493-98 (7th Cir. 1984); *see also* Barton B. Clark, Comment, *Give 'Em Enough Rope: States, Subdivisions, and the Market Participant Exception to the Dormant Commerce Clause*, 60 U. CHI. L. REV. 615, 627-28 (1993) (suggesting that courts should measure the autonomy of a state's local governments to determine the constitutionality of state-mandated preference laws).

52. *W.C.M. Window*, 730 F.2d at 495 ("The 'market participant' is the school board, just as the market participant in *White* was the city of Boston. The state is the regulator, telling thousands of local government units that they must not give construction contracts to employers of nonresidents.").

53. 460 U.S. 204 (1983).

54. Interestingly, the executive order was based on a Massachusetts law that required each county, town, or district to prefer veterans and residents in hiring for public construction projects. *See* 460 U.S. at 224 n.8 (Blackmun, J., concurring in part and dissenting in part)

mayor's order reached beyond market participation because it interfered with the contractual relations of two private parties — public contractors and their employees. The Supreme Court responded that “the Commerce Clause does not require the city to stop at the boundary of formal privity of contract” because “[e]veryone affected by the order is, in a substantial if informal sense, ‘working for the city.’”⁵⁵ Therefore, it appears that formal privity between the contracting parties and the state is not necessary for the market-participant exception to apply to state-mandated preference laws.⁵⁶

Another potential and related problem with treating state and local governments as a single market participant is that state-mandated preference laws appear to operate like the regulations that the Court struck down in *South-Central Timber Development v. Wunnicke*.⁵⁷ As mentioned earlier,⁵⁸ *South-Central* limits the ability of states to impose “downstream restrictions” on its contracting partners, thereby effecting separate, private economic relationships. Because state-mandated preference laws restrict the ability of local governments to contract with construction workers and firms, arguably such state laws pose invalid restrictions on the “downstream” local hiring market. A simple, but probably unsatisfying and somewhat circular, answer to this problem is that under the “arm-of-the-state” dependency theory, courts can view the state’s mandated preference law as essentially affecting the state’s own contractual relationships rather than those of a separate “downstream” entity. Thus, measuring the dependence or autonomy of local governments to determine whether the market-participant ex-

(citing MASS. GEN. LAWS ANN. ch. 149, § 26 (West 1982)). The Massachusetts Supreme Court also struck down this law when it invalidated the mayor’s executive order. See *Massachusetts Council of Constr. Employers v. Mayor of Boston*, 425 N.E.2d 346, 352-53 (Mass. 1981). Because the Commonwealth did not appeal this part of the lower decision, the Supreme Court did not decide the issue of whether a state-mandated preference is constitutional. 460 U.S. at 224 n.8 (Blackmun, J., concurring in part and dissenting in part).

55. 460 U.S. at 211 n.7. But see 460 U.S. at 223 (Blackmun, J., concurring in part and dissenting in part) (arguing that “[t]he ‘sense’ in which those affected by the Mayor’s order ‘work for the city’ . . . lack[s] substance altogether” because the state does not hire, fire, pay, or negotiate with construction workers or subcontractors).

56. Cf. *Trojan Technologies v. Pennsylvania*, 916 F.2d 903, 911 (3d Cir. 1990), cert. denied, 501 U.S. 1212 (1991) (arguing by analogy that under a state-mandated preference law, suppliers of a local government are “supplying for the state”). The two situations are not perfectly analogous, however. The Supreme Court relied in *White* on the fact that the city was spending its own money. *White*, 460 U.S. at 214-15 (“Insofar as the city expended its own funds in entering into construction contracts for public projects, it was a market participant . . .”). In *White*, the public contractor acted almost like an intermediary agent for the local government, which supplied the actual payroll. Under some state-mandated preference laws, however, the state government does not supply funds, at least directly, to carry out the preferences.

57. 467 U.S. 82 (1984).

58. See *supra* notes 38-40 and accompanying text.

ception applies to state-mandated preference laws would be consistent with current market-participant case law.

A more complex, and more satisfactory, answer to whether state-mandated preference laws constitute downstream restrictions would require an examination of the rationales that justify the market-participant exception to the dormant Commerce Clause. For the market-participant exception to be what it purports to be — an exception to the dormant Commerce Clause — it must reflect the balance of values underlying the dormant Commerce Clause. The dormant Commerce Clause protects the states' ability to enact legitimate regulatory measures.⁵⁹ At the same time, it exists to prevent trade wars and economic balkanization.⁶⁰ Consequently, the rationales for the market-participant exception must allow only legitimate regulations that do not excessively burden interstate commerce. If these rationales apply to state-mandated preference laws, then such laws should be constitutional under the market-participant exception. If these rationales do not apply, however, then courts should strike such laws down as impermissible downstream restrictions.

II. STATE-MANDATED PREFERENCE LAWS, STATE-LOCAL RELATIONSHIPS, AND THE RATIONALES FOR THE MARKET-PARTICIPANT EXCEPTION TO THE DORMANT COMMERCE CLAUSE

Although the market-participant exception to the dormant Commerce Clause seems to represent an appropriate accommodation to state regulatory power in the abstract, defining its exact justification and scope has confounded the Supreme Court and numerous commentators. In fact, many commentators have urged the Court to abolish the exception.⁶¹ Nevertheless, two rationales

59. See *supra* notes 25, 28 and accompanying text.

60. See *supra* note 22 and accompanying text.

61. See *South-Central Timber Dev. v. Wunnicke*, 467 U.S. 82, 101 (1984) (Brennan, J., concurring) ("In my view, Justice White's treatment of the market-participant doctrine and the response of Justice Rehnquist point up the inherent weakness of the doctrine."); *Swin Resource Sys. v. Lycoming County*, 883 F.2d 245, 262 (3d Cir. 1989) (Gibbons, C.J., dissenting); Theodore Y. Blumoff, *The State Proprietary Exception to the Dormant Commerce Clause: A Persistent Nineteenth Century Anomaly*, 1984 S. ILL. U. L.J. 73, 76-77; A. Dan Tarlock, *National Power, State Resource Sovereignty and Federalism in the 1980's: Scaling America's Magic Mountain*, 32 U. KAN. L. REV. 111, 133 (1983); Timothy P. Collins, Case-note, 27 WAYNE L. REV. 1575, 1590 (1981); Carol A. Fortine, Note, *The Commerce Clause and Federalism: Implications for State Control of Natural Resources*, 50 GEO. WASH. L. REV. 601 (1982); Greer L. Phillips, Comment, *Commerce Clause Immunity for State Proprietary Activities: Reeves, Inc. v. Stake*, 4 HARV. J.L. & PUB. POLY. 365 (1981); Adam B. Schiff, Comment, *State Discriminatory Action Against Nonresidents: Using the Original Position Theory as a Framework for Analysis*, 22 HARV. J. ON LEGIS. 583, 587 (1985); William L. Thorpe, Note, *State Purchasing Activity Excluded from Commerce Clause Review — Hughes v. Alexandria Scrap Corp.*, 18 B.C. IND. & COMM. L. REV. 893, 901 (1977).

have emerged that both justify the market-participant exception and define its scope — the moral and political entitlement of state residents to the benefit of state funds and the built-in spending restraints of resident contractual preference laws. These two rationales identify how resident preference laws have a legitimate justification and how they do not always burden commerce excessively.

Section II.A describes these rationales in detail and argues that they provide a benchmark against which courts should evaluate whether the market-participant exception applies to state-mandated preference laws. Section II.B then applies these two rationales to state-mandated preference laws and concludes that although not all such laws are justifiable under these rationales, the market-participant exception should nevertheless apply to some state-mandated preference laws. Section II.C argues, however, that the current application of the market-participant exception to state-mandated preference laws — by focusing on state-local relationships — fails to adequately distinguish between laws that comport with the rationales of the market participant exception and those that do not. This section demonstrates the need for courts to develop a different application of the market-participant exception to state-mandated preference laws.

A. *The Rationales for the Market-Participant Exception*

The Supreme Court and various legal commentators have suggested many possible rationales for the market-participant exception to the dormant Commerce Clause. Only two of these rationales, however, actually justify the exception *and* define its scope. First, preferring residents when spending their money is a legitimate state objective as a matter of moral and political theory. Second, preferences that require the expenditure of state funds have built-in restraints that may make them less politically and economically divisive than other discriminatory state laws. Both of these rationales actually focus on the concerns of the dormant Commerce Clause — protecting legitimate regulation while avoiding excessive burdens on interstate commerce. The other rationales either fail to provide sufficient guidance for lower courts to define the limits of the exception, or they fail completely to justify the exception.

The Supreme Court itself may have misgivings about the market-participant exception. In *New Energy Co. v. Limbach*, 486 U.S. 269 (1988), the Court held that a tax credit given by the state of Ohio to promote the sale of ethanol fell under the state's "distinctive governmental capacity," making the market-participant exception inapplicable. 486 U.S. at 277. The solution, however, is not to replace one empty label — "market participant" — with another — "distinctive governmental capacity."

Moral and political theory suggests that states may legitimately prefer their own citizens in public contracting because they are spending state funds. The money that states spend comes mostly from residents through various taxes, tolls, and levies. Thus, these residents have a greater claim to the benefit of these resources than nonresidents do.⁶² Some commentators have referred to this justification as the "sow-and-reap" rationale⁶³ or the "Lockean labor-desert theory,"⁶⁴ because the residents have labored to earn money that they then "sow" in the form of taxes to the state. When the state later spends this "sown" money, residents deserve to "reap" the benefits of those expenditures. In other words, states should be able to allocate expenditures of state funds to residents before nonresidents. Other forms of interstate discrimination, such as taxes and tariffs on nonresidents, do not require the state to spend any

62. See *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980):

The State's refusal to sell to buyers other than South Dakotans is "protectionist" only in the sense that it limits benefits generated by a state program to those who fund the state treasury and whom the State was created to serve. . . . Such policies, while perhaps "protectionist" in a loose sense, reflect the essential and patently unobjectionable purpose of state government — to serve the citizens of the state.

447 U.S. at 442; see also Dan T. Coenen, *Untangling the Market-Participant Exemption to the Dormant Commerce Clause*, 88 MICH. L. REV. 395, 421 (1989); Regan, *supra* note 29, at 1194-95; Jonathan D. Varat, *State "Citizenship" and Interstate Equality*, 48 U. CHI. L. REV. 487, 523 (1981).

Professor Laurence Tribe has offered a variation on this theory that focuses on whether the state "created" the commerce at issue. LAURENCE H. TRIBE, *CONSTITUTIONAL CHOICES* 146 (1985) ("The principle that necessarily underlies the market participant-market regulator distinction is that, when the state is *creating* commerce that would otherwise not exist, it has greater freedom to *shape* that commerce than when it is merely *intruding* into a previously existing market."). The Supreme Court, however, expressly rejected this rationale in *Reeves*, 447 U.S. at 446 n.18, and some commentators have criticized its explanatory power. See Coenen, *supra*, at 410-13 (arguing that Professor Tribe's commerce creation rationale is underinclusive because it cannot explain *Alexandria Scrap* and *Reeves*).

Another variation that exists on this rationale involves treating the state like a "private actor" because it is spending its own money. See, e.g., Clark, *supra* note 51, at 627-28; William L. Kovacs & Anthony A. Anderson, *States as Market Participants in Solid Waste Disposal Services — Fair Competition or the Destruction of the Private Sector?*, 18 ENVTL. L.J. 779, 803 (1988); see also *Reeves, Inc. v. Stake*, 447 U.S. 429, 438-39 (1980) (arguing, in support of the market-participant exception, that states have the same right as private parties to choose their trading partners and that states face the same limitations as private market participants). Professor Tribe points out that there is a certain irony in using the private-party image to justify the state's ability to promote the welfare of its citizens. See TRIBE, *supra* note 5, § 6-11, at 432. Moreover, Professor Karl Mannheim observes that analogizing state activity to private behavior might spawn exceptions, such as the state as monopolist. See Karl Mannheim, *New-Age Federalism and the Market-Participant Doctrine*, 22 ARIZ. ST. L.J. 559, 608 (1990); cf. Clark, *supra* note 51, at 629-32 (applying antitrust concepts to the private party model). Ultimately, the "private party" label seems as conclusory as the current "market participant" label because it fails to account for the rationales supporting the market-participant exception.

63. Coenen, *supra* note 62, at 421-26.

64. Varat, *supra* note 62, at 522-23. Professor Varat recognizes that limitations may exist on a state's ability to exclude nonresidents on this rationale. If a state possesses an overabundance of resources and exclusion of nonresidents will unnecessarily disrupt the economy, the resident preference should be impermissible. This is particularly true when the nonresident offers to pay her fair share of state taxes. *Id.* at 531-36.

taxpayer-contributed money. Therefore, preferential state spending is more legitimate morally and politically than discriminatory taxes or tariffs.

Contractual preferences for residents are also less likely than other discriminatory regulations to place excessive burdens on interstate commerce. Discriminatory taxes and tariffs appear to cost the state very little to enact or administer because they either produce income or merely reduce tax revenues.⁶⁵ Contractual preferences and subsidies,⁶⁶ conversely, have, as Professor Donald Regan has argued, built-in restraints because they require the expenditure of limited state funds.⁶⁷ This means that contractual preferences will be more expensive to create and administer than discriminatory taxes and tariffs, so they are more likely to be limited in scope.⁶⁸ In addition, discriminatory taxes and tariffs encourage retaliation from other states, creating a "race-to-the-bottom" situation that might eventually hamper or destroy free trade.⁶⁹ Contractual preferences are less likely to engender such retaliation because other states may recognize the political legitimacy of a state preferring its own residents with state funds.⁷⁰ Both the "expensiveness" of spending preferences and the lesser likelihood of retaliation are "built-in restraints" in the sense that they are natural components of spending preferences that pose less of a burden on interstate commerce than other discriminatory measures.

Naturally, neither of these rationales justifies all contractual preferences. In many instances, the state may be spending money that it cannot completely attribute to its own residents. For exam-

65. In fact, most discriminatory measures rarely have beneficial effects and often impose administrative and efficiency costs that states can never recoup. See, e.g., PAUL A. SAMUELSON, *ECONOMICS* 679 (10th ed. 1977) (making this argument in the context of international trade).

66. Although the Supreme Court has never had to decide whether subsidies are constitutional under the dormant Commerce Clause, it has indicated general approval of such measures. See, e.g., *West Lynn Creamery, Inc. v. Healy*, 114 S. Ct. 2205, 2214 & n.15 (1994); *New Energy Co. v. Limbach*, 486 U.S. 269, 278 (1988); see also *West Lynn Creamery*, 114 S. Ct. at 2220 (Scalia, J., concurring) (arguing that the Court implicitly upheld subsidies in a market-participant case, *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976)). But see Regan, *supra* note 29, at 1196 (arguing that the Court should not uphold subsidies because such measures can easily distort the market).

67. See Regan, *supra* note 29, at 1194-95. Of course, even contractual preferences create economic inefficiency. See, e.g., Donald E. Jordan, Comment, *In-State Preferences in Public Contracting: States' Rights Versus Economic Sectionalism*, 49 U. COLO. L. REV. 205, 216 (1978) (discussing the questionable benefits of contractual preferences). A simple example can help demonstrate this phenomenon. If a nonresident can complete a contract for \$100,000, whereas a resident will charge \$120,000, then a resident preference will create an inefficiency of \$20,000 on the contract.

68. See Coenen, *supra* note 62, at 434-35 (stating that while discriminatory taxes and subsidies are also "expensive," the costs are often hidden; thus, residents will be more likely to vote for such laws than for contractual preferences); Regan, *supra* note 29, at 1194-95.

69. See RICHARD A. EPSTEIN, *BARGAINING WITH THE STATE* 127-30 (1993).

70. See Coenen, *supra* note 62, at 433-44; Regan, *supra* note 29, at 1194-95.

ple, the money may come from federal subsidies or from taxes or licensing fees paid by nonresidents. Moreover, even when the state is spending money derived from its own residents for contractual preferences, some economic inefficiencies will result, and other states still may retaliate with their own discriminatory preferences, taxes, or subsidies.⁷¹ Consequently, courts should strike down those contractual preferences that create large inefficiencies or unnecessarily risk retaliation. Nevertheless, these two rationales explain why it is logical in light of the concerns underlying the dormant Commerce Clause to use a mechanism like the market-participant exception to differentiate at least some contractual preferences from other discriminatory measures.

Two other rationales for the market-participant exception do provide some theoretical support for exception, but they fail to define its scope clearly and thus they fail to provide any guidelines for lower courts. First, the Supreme Court has stated that the political nature of state proprietary activity makes congressional action more appropriate than judicial intervention.⁷² Second, the Court has expressed concern that restraining the states' ability to enact preference laws would impinge on their traditional role as experimental laboratories.⁷³ Both of these rationales — essentially encouraging judicial restraint and respect for federalism — are appropriate considerations in light of the entitlement and built-in restraint rationales discussed above. Because residents are more entitled to the benefit of their own resources, courts should be more reluctant to strike resident-preference laws down. In addition, because these laws have fewer negative effects on interstate commerce, states should have greater freedom to enact such laws and structure them in ways most beneficial to state residents.

Neither of the Supreme Court's rationales, however, provides a satisfactory guide to distinguishing between constitutional and unconstitutional preference laws. As Professor Dan Coenen observes, a general policy of judicial restraint under the dormant Commerce Clause "might equally well justify judicial noninterference with

71. See *supra* note 64.

72. See *Reeves, Inc. v. Stake*, 447 U.S. 429, 439 (1980); cf. *Wisconsin Dept. of Indus., Labor & Human Rel. v. Gould, Inc.*, 475 U.S. 282, 286-91 (1986) (stating that Congress can reverse market-participant rulings). Commentators have differed over whether dormant Commerce Clause jurisprudence calls for judicial restraint or whether it actually calls for judicial activism. Compare Coenen, *supra* note 62, at 439 (arguing that the possibility of congressional preemption does provide a weak "background" justification for judicial restraint if other factors counsel a cautious approach) with *TRIBE*, *supra* note 5, § 6-2, at 404 (contending that the "blend of judicial and legislative activity" that characterizes dormant Commerce Clause jurisprudence actually encourages judicial activism).

73. See *Reeves*, 447 U.S. at 441; see also *TRIBE*, *supra* note 5, § 6-11, at 434 (stating that the market-participant exception "usher[ed] in a new day of federalism"); Coenen, *supra* note 62, at 441 (observing the importance of federalism, experimentation, and "optimal responsiveness to local concerns").

state regulatory and tax programs that discriminate against interstate commerce,"⁷⁴ but such discriminatory measures are clearly unconstitutional. General notions of respect for federalism encounter the same problem. In a spirit of economic "experimentation," states could enact preference laws whose burdensome effects on commerce far outweigh the legitimacy of the residents' entitlement to state funds. Neither a general policy of judicial restraint or of respect for federalism could explain why the Court upheld Boston's resident preference law in *White v. Massachusetts Council of Construction Employers*⁷⁵ and struck down Alaska's primary-manufacture requirement in *South-Central Timber Development v. Wunnicke*.⁷⁶

Finally, some commentators have attempted to justify the market-participant exception on economic theory grounds. They assert that contractual preference laws encourage states to spend resources on public contracts, whereas forcing states to spend their funds on nonresidents imperils such spending.⁷⁷ Professor Mark Gergen further argues that resident-preference laws can actually encourage efficiency because such laws force states to internalize the costs of their actions.⁷⁸ These arguments appear neither compelling nor accurate. Although economic prosperity is an important value under the Commerce Clause, the Court has always rejected efforts at interstate discrimination when motivated merely by economic gain.⁷⁹ Moreover, resident preferences often cause more economic harm than good,⁸⁰ and are as likely to be the result of

74. Coenen, *supra* note 62, at 439.

75. 460 U.S. 204 (1983).

76. 467 U.S. 82 (1984).

77. See Mark P. Gergen, *The Selfish State and the Market*, 66 TEXAS L. REV. 1097, 1112 (1988); see also Regan, *supra* note 29, at 1194-95.

78. See Gergen, *supra* note 77, at 1111.

79. See *supra* note 26 and accompanying text; see also *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 92 (1987) ("The Constitution does not require the states to subscribe to any particular economic theory."); Thomas K. Anson & P. M. Schenkkan, *Federalism, the Dormant Commerce Clause, and State-Owned Resources*, 59 TEXAS L. REV. 71, 78 n.31 (1980) ("The assumption that the commerce clause embodies a free trade value . . . is erroneous"); Julian N. Eule, *Laying the Dormant Commerce Clause to Rest*, 91 YALE L.J. 425, 434 (1982) ("The commerce clause . . . cannot be said to establish and protect free trade or a national marketplace as a fundamental constitutional value.").

80. See *supra* notes 65, 67 and accompanying text. Despite his general encouragement of resident preferences, Professor Gergen suggests that resident buying and hiring preferences should be *per se* illegal because they are "impure" subsidies. Gergen, *supra* note 77, at 1134. Unfortunately, he never fully explains this distinction, particularly when he states that preference programs like that in *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204 (1983), "fall well within the principle that a state may limit the benefits of public programs." Gergen, *supra* note 77, at 1141. Perhaps his aversion to such preferences derives from a concern that they promote political favoritism and undermine basic principles of free trade and private ownership: "Would we really permit a socialist government in Vermont to defeat free trade by collectivizing its retail establishments, factories, and towns?" *Id.* at 1143.

parochial politics as of rational decisionmaking.⁸¹ Hence, it is unlikely that such preferences will maximize economic welfare.

Therefore, the only two rationales that justify the market-participant exception and define its scope are the moral and political entitlement of state residents to the benefit of state funds and the built-in spending restraints of resident preference laws. Applying these two rationales may result in judicial restraint and respect for federalism on occasion, but these latter two rationales cannot determine when such restraint or respect is in fact desirable and when it is not.

B. *Market-Participant Theory and State-Mandated Preference Laws*

Although some state-mandated preference laws may not satisfy the two justifications for the market-participant exception — the entitlement and built-in restraints rationales — many others will. Thus, courts should not categorically reject applying the market-participant exception to such laws. In the language of the market-participant cases, some state-mandated laws should be impermissible “downstream restrictions” while others should be permissible “market participation.”

Many state-mandated preference laws have the same legitimacy under the entitlement theory as preference laws that operate on just the state level. When local governments spend funds in accordance with a state-mandated preference law, those governments are still spending money contributed by residents. Professor Coenen has argued that the “sow-and-reap” rationale only partially supports state-mandated preference laws because the state is not distributing money that is “fairly attributable to all residents of the state.” Instead, he argues that such laws require local governments to spend their “own” money in certain ways.⁸² While this is true, it should not be a fatal concern under the dormant Commerce Clause. One of the main evils the dormant Commerce Clause exists to prevent is discrimination against nonresidents who are politically powerless to influence the policies of the discriminating state.⁸³ Residents living

81. See *Reeves, Inc. v. Stake*, 447 U.S. 429, 450 (1980) (Powell, J., dissenting) (“A State frequently will respond to market conditions on the basis of political rather than economic concerns.”); see also Phillips, *supra* note 61, at 378; Note, *Home-State Preferences in Public Contracting: A Study in Economic Balkanization*, 58 IOWA L. REV. 576, 585 (1973); *supra* note 80.

82. Coenen, *supra* note 62, at 483 n.497. Professor Coenen also argues that concerns of federalism and state experimentation diminish under state-mandated preference laws because local governments become less able to respond to the local will. *Id.* He notes, however, that traditional concerns of federalism surround the state’s ability, and not that of local governments, to experiment with different policies. *Id.*

83. See *supra* note 27 and accompanying text.

under a particular local government, unlike nonresidents of the state, are not politically powerless. These residents can petition the state to eliminate state-mandated preference laws if they feel that other residents who have not contributed to local government funds are unfairly benefitting from such funds. As long as the state is directing funds supplied in some way by residents, rather than taking funds from nonresidents, then the entitlement rationale should still apply. This result is particularly true if the state has supplied some or all of the local government's funding.

Many state-mandated preference laws also do not place a larger burden on commerce than a preference law that only applies to the state government. There are two ways in which such laws could present a greater burden. First, state-mandated preference laws do not have as strong a built-in "expensiveness" restraint on their enactment. Particularly when the state is directing the expenditure of funds raised by local governments, such laws will not be as expensive to the state because it is not spending funds from its own treasury.⁸⁴ Second, state-mandated preference laws could potentially affect a far greater number of contracting parties than merely state-level preferences because local governments are responsible for most public contracting.⁸⁵ States need not enact state-mandated preference laws that operate so broadly, however. There are a number of ways to limit the operation of a state-mandated preference law that would greatly reduce the burden on interstate commerce that such a law might pose, such as imposing geographical or temporal limitations on the law.⁸⁶ Such limitations could produce a state-mandated preference law that is far less burdensome than state-level preference laws currently upheld under the market-participant exception.

Therefore, rather than rejecting state-mandated preferences categorically, as at least one commentator has advocated,⁸⁷ courts should seek to distinguish between those laws that fit within the rationales for the market-participant exception — thus constituting

84. See Coenen, *supra* note 62, at 483.

85. See *W.C.M. Window Co. v. Bernardi*, 730 F.2d 486, 496 (7th Cir. 1984) (stating that state-mandated preference laws "could do great damage to the principles of free trade on which the negative commerce clause is based" because local governments do far more contracting than state governments). But see *Trojan Technologies v. Pennsylvania*, 916 F.2d 903 (3d Cir. 1990), *cert. denied*, 501 U.S. 1212 (1991):

It may be true that local municipalities and authorities are responsible for the great bulk of sub-national public procurement. However, we find no suggestion in the Supreme Court's previous forays into this area that the quantum of market purchases should affect a public entity's qualification for market participant status.
916 F.2d at 911.

86. See *infra* notes 118-20 and accompanying text.

87. See Coenen, *supra* note 62, at 483 (arguing tentatively that state-mandated preference laws should always violate the dormant Commerce Clause).

valid “market-participation” — and those that do not — thus constituting impermissible “downstream restrictions.” Part III refines the market-participant exception to handle this task, drawing on dormant Commerce Clause and Privileges and Immunities case law. Before that, however, section II.C explains why the current interpretation of the market-participant exception, which focuses on the relationship between states and their local governments, fails to distinguish valid state-mandated preference laws from invalid ones.

C. *Market-Participant Theory and State-Local Relationships*

Under current market-participant doctrine, courts have evaluated the constitutionality of state-mandated preference laws based on whether they characterize the relationship between a state and its local governments as one of dependence or independence.⁸⁸ Following the traditional approach, courts assume that local governments are “creatures of the state” and that states enacting state-mandated preferences laws “through” them are market-participants.⁸⁹ The more contemporary approach requires courts to determine the actual independence of local governments, calling the state a market participant only when it is mandating the contracting of dependent local governments.⁹⁰ Neither approach, however, allows courts to distinguish between legitimate, less burdensome state-mandated preference laws and those that excessively burden interstate commerce.

The traditional approach to state-local relationships completely fails to evaluate state-mandated preference laws in terms of the justifications for the market-participant exception. By assuming dependence, this approach concludes that all state-mandated preference laws are valid under the dormant Commerce Clause. However, some state-mandated preference laws may dictate the use of money that is not fairly attributable to the state. In cases in which the federal government has provided the lion’s share of funding, or in which nonresidents have contributed to the state’s funds through taxes and licensing fees, residents do not have the justification for favoring themselves in public contracting. Furthermore, some preference laws may have such widespread effects that courts should strike them down despite any such justification. The traditional approach to state-local relationships would allow the state to tell every single city, county, municipality, school board, or other political subdivision, to hire only residents, to buy only goods made by residents, and to sell goods made with state funds only to residents for any length of time and for any reason. The scope of this

88. See *supra* section I.C.

89. See *supra* notes 45-46 and accompanying text.

90. See *supra* notes 51-52 and accompanying text.

preferential treatment would dwarf other forms of discrimination that the court has struck down under the dormant Commerce Clause.⁹¹

The more contemporary approach to state-local relationships does not fare much better. This approach at least condemns some state-mandated preference laws as violating the dormant Commerce Clause — namely those that act on autonomous local governments. The distinction this approach draws, however, has little to do with the legitimacy of the state's action or the potential burden on interstate commerce. Moreover, the test for determining autonomy is susceptible to manipulation by state legislatures. They ultimately control the distribution of power within the state, and they could alter the balance whenever they wished to create a "dependent" local government from one that was formerly "autonomous."⁹² Even the best test for determining autonomy in the dormant Commerce Clause context would not produce results that comport with the justifications for the market-participant exception. The best test would probably focus on the amount of financial support that the state has supplied because residents can definitely claim a legitimate entitlement to state funds that are merely spent through local governments. Yet, this test would fail to strike down

91. See *supra* notes 7, 26 and accompanying text.

92. Even if courts treated the issue of local government autonomy as a federal one, state law would undoubtedly influence their finding. In the areas in which courts already attempt to measure local government autonomy, see *supra* notes 47-50 and accompanying text, they primarily look to state law for guidance. See, e.g., *Lake Country Estates v. Tahoe Regional Planning Agency*, 440 U.S. 391, 401-02 (1979) (balancing six factors: 1) the state's designation of the agency; 2) the relative power of appointment between the state and the agency; 3) the agency's funding; 4) the nonbinding aspect of the agency's obligations; 5) the agency's primary mission; and 6) the state's lack of veto power over agency rules); *Mt. Healthy City Sch. Dist. Bd. of Educ. v. Doyle*, 429 U.S. 274, 280 (1977) (balancing four factors: 1) the state's designation of the school board; 2) the degree of state supervision; 3) the level of state funding; and 4) the school board's capacity to generate revenue); see also Alex E. Rogers, Note, *Clothing State Governmental Entities with Sovereign Immunity: Disarray in the Eleventh Amendment Arm-of-State Doctrine*, 92 COLUM. L. REV. 1243, 1269 (1992) (summarizing the factors employed by lower courts into five categories: 1) the entity's functions; 2) the degree of state control; 3) the entity's powers, especially fiscal autonomy; 4) the state's designation of the entity; and 5) the financial liability of the state for the entity's legal violations).

Another, albeit less important, argument against attempts to measure local government autonomy is that such attempts have met with little success. See ERWIN CHEMERINSKY, *FEDERAL JURISDICTION* § 7.4, at 387 (2d ed. 1994) (stating that "the law concerning the [11th Amendment] immunity of state agencies, boards, and other entities . . . is quite inconsistent"); Rogers, *supra*, at 1269 (stating that "the courts craft disparate tests and rely upon vague factors, thereby generating conflicting results"). A prime example of such conflict occurred when the Second and Third Circuit Courts of Appeals split on whether the Port Authority of New York and New Jersey was a dependent political subdivision or an autonomous entity for the purposes of the Eleventh Amendment. See *Feeney v. Port Auth. Trans-Hudson Corp.*, 873 F.2d 628 (2d Cir. 1989), *affd. on other grounds*, 495 U.S. 299 (1990); *Port Auth. Police Benevolent Assn. v. Port Auth.*, 819 F.2d 413 (3d Cir.), *cert. denied*, 484 U.S. 953 (1987). The Supreme Court eventually decided this issue in *Hess v. Port Authority Trans-Hudson Corp.*, 115 S. Ct. 394 (1994).

those state-mandated preference laws that impose excessive burdens on interstate commerce despite the claim of entitlement. In addition, this test would fail to allow state-mandated preference laws that operate completely on local funding but that pose little threat to interstate commerce.

Ultimately, focusing on the relationship between the state and its local governments has little to do with the concerns of the dormant Commerce Clause. The dormant Commerce Clause protects legitimate regulations that do not pose an excessive burden to interstate commerce. The traditional approach ignores both of these concerns. The more contemporary approach, if crafted and applied properly, would at least protect the state's legitimate ability to prefer its own residents in some instances, but it does so without any reference to the burden on interstate commerce. Therefore, courts must develop a different approach to evaluating the constitutionality of state-mandated preference laws that comports with the rationales for the market-participant exception as identified in this Note.

III. APPLYING THE MARKET-PARTICIPANT EXCEPTION TO STATE-MANDATED PREFERENCE LAWS

Some commentators have urged courts to apply the market-participant exception to the dormant Commerce Clause in a more substantive manner.⁹³ This Note similarly argues that courts should apply the market-participant exception with reference to the rationales identified in this Note that justify and define the scope of the exception. Fortunately, there is already some guidance within the law to help craft such an approach. A more substantive approach to the market-participant exception can draw upon the Supreme Court's long-standing jurisprudence under the dormant Commerce Clause and also that of the Privileges and Immunities Clause.

Privileges and Immunities Clause doctrine provides a particularly apt analogy to dormant Commerce Clause doctrine, at least with respect to issues of interstate economic discrimination. The two clauses have similar historical origins.⁹⁴ In addition, cases

93. See *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204, 218 (Blackmun, J., concurring in part and dissenting in part) ("The line between regulation and market participation, for purposes of the Commerce Clause, should be drawn with reference to the constitutional values giving rise to the market participant exemption itself."); Coenen, *supra* note 62, at 398 (arguing that courts should examine the "competing constitutional values" underlying the market-participant cases); Regan, *supra* note 29, at 1196-97 (arguing that courts should engage in line-drawing based on the criteria of whether the state is spending its own money in order to determine whether the market-participant applies to a particular state activity).

94. The Framers derived both clauses from the fourth article of the Articles of Confederation, which was to "secure and perpetuate mutual friendship and intercourse among the people of different States." *TRIBE, supra* note 5, § 6-35, at 537 (quoting ART. CONFED. art. IV); see also *Hicklin v. Orbeck*, 437 U.S. 518 (1978) (stating that the clauses have a "shared

under the Privileges and Immunities Clause recognize that states are entitled to favor their own residents when spending residents' money.⁹⁵ Furthermore, these cases also recognize that the Privileges and Immunities Clause protects against the economic and political balkanization that discrimination against nonresidents often causes.⁹⁶ Logically, these cases produce the same balance that exists under the dormant Commerce Clause — governments can favor their own citizens when they are spending state money but they are limited in the extent to which they can do so.⁹⁷

vision of federalism"). At least one commentator has argued that the modern dormant Commerce Clause actually fulfills the role envisioned by the Framers for the Privileges and Immunities Clause. See Eule, *supra* note 79, at 446-55; see also Charles L. Black, Jr., *Perspectives on the American Common Market*, in REGULATION, FEDERALISM, AND INTERSTATE COMMERCE 59, 65 (A. Dan Tarlock ed. 1981). But see Regan, *supra* note 29, at 1202-06 (arguing that sufficient distinctions exist between the Commerce Clause and the Privileges and Immunities Clause to maintain separate bodies of doctrine).

There is one significant historical difference between the two clauses. Corporations may not sue under the Privileges and Immunities Clause because, under that clause, they do not qualify as citizens. *Western & S. Life Ins. Co. v. State Bd. of Equalization*, 451 U.S. 648, 665 (1981); *Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 177, 181 (1869) (suggesting in dicta that the term "citizens" in the Privileges and Immunities Clause refers only to natural persons"). But see Eule, *supra* note 79, at 451 (arguing that the "legal underpinnings" of this rule are "no longer sound"); Martin H. Redish and Shane V. Nugent, *The Dormant Commerce Clause and the Constitutional Balance of Federalism*, 1987 DUKE L.J. 569, 610-11 ("From a policy perspective, there can be little doubt that corporations should receive the protection of the privileges and immunities clause.").

95. Under the Privileges and Immunities Clause, the Supreme Court has allowed states to prefer residents in public education, see *Martinez v. Bynum*, 461 U.S. 321 (1983), public welfare programs, see *Shapiro v. Thompson*, 394 U.S. 618 (1969) (striking down a one-year residency requirement for welfare benefits not because of the requirement itself but because of its unjustified duration), and hiring for public construction jobs, see *United Bldg. & Constr. Trades Council v. Mayor of Camden*, 465 U.S. 208 (1984). In *United Building*, the Court explicitly recognized this justification:

The fact that Camden is expending its own funds or funds it administers in accordance with the terms of a grant is certainly a factor — perhaps the crucial factor — to be considered in evaluating whether the statute's discrimination violates the Privileges and Immunities Clause. . . .

. . . States should have considerable leeway in analyzing local evils and in prescribing appropriate cures." This caution is particularly appropriate when a government body is merely setting conditions on the expenditure of funds it controls. 465 U.S. at 221-23 (citation omitted) (quoting *Toomer v. Witsell*, 334 U.S. 385, 396 (1948)); see also TRIBE, *supra* note 5, § 6-35, at 541 (observing that state creation of a resource or other good would remain a powerful argument for justifying discrimination under the Privileges and Immunities Clause).

96. See *Baldwin v. Montana Fish & Game Commn.*, 436 U.S. 371, 388 (1978) (stating that the clause protects the "maintenance or well-being of the Union"); *Austin v. New Hampshire*, 420 U.S. 656, 660-61 (1975) (stating that the Framers created the clause to safeguard "all the privileges of trade and commerce") (quoting ART. CONFED. art. IV).

97. As Professor Tribe observes:

Police and fire departments are quintessentially creatures of the state, supported by state or local revenue and operated for the good of the local citizenry, yet it is inconceivable that a state would be permitted to deny police and fire protection to tourists or short-term visitors, or to charge a premium to those just passing through for the service of extinguishing a blaze or apprehending a hit-and-run perpetrator. Discrimination against non-residents with respect to such basic advantages of civilization would surely undermine national cohesion and deter intercourse among the states.

Section III.A describes how courts can refine their approach to state-mandated preference laws under the market-participant exception with guidance from case law under the dormant Commerce Clause and the Privileges and Immunities Clause. Section III.B then applies this approach to the federal cases that have split on the constitutionality of state-mandated preference laws.

A. *A More Substantive Application of the Market-Participant Exception*

Any application of the market-participant exception should take into account the two rationales that support and define the scope of the exception — entitlement and built-in restraints. This approach will guarantee that market-participant decisions rest on substantive analysis rather than on blind labeling. Moreover, this approach conforms naturally to traditional dormant Commerce Clause and Privileges and Immunities analysis.

Because the market-participant exception derives from dormant Commerce Clause jurisprudence, the latter provides a ready guide for the former. Dormant Commerce Clause analysis consists of two parts. First, courts look for a legitimate purpose for the state regulation.⁹⁸ Second, they balance the local benefits achieved by the regulation against the burden it imposes on interstate commerce.⁹⁹ Under the justifications for the market-participant exception, states have a legitimate purpose when enacting contractual preferences — they can prefer residents when they spend funds contributed by those residents. Moreover, the built-in restraints on state spending make preference laws less likely to burden commerce substantially. Thus, on balance, courts should be willing to uphold *some* preference laws, whereas they should *always* strike down other discriminatory measures, such as discriminatory taxes on nonresidents. The Supreme Court has at least implicitly condoned this reasoning in the dormant Commerce Clause context by upholding under the market-participant exception state laws that prefer residents when buying scrap metal,¹⁰⁰ selling state-produced cement,¹⁰¹ and hiring

TRIBE, *supra* note 5, § 6-35, at 540-41 (footnotes omitted). The Supreme Court has stated, however, that current market-participant doctrine is not in harmony with current privileges and immunities doctrine in this regard. See *United Bldg.*, 465 U.S. at 220 ("This concern with comity [under the Privileges and Immunities Clause] cuts across the market regulator-market participant distinction that is crucial under the Commerce Clause.").

98. See *supra* notes 24-25 and accompanying text.

99. See *supra* notes 29-30 and accompanying text.

100. See *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976).

101. See *Reeves, Inc. v. Stake*, 447 U.S. 429, 439 (1980).

construction workers,¹⁰² while striking down other discriminatory regulations that do not involve state spending.¹⁰³

Although this balancing approach is merely implicit in the Supreme Court's market-participant cases, the Court explicitly performs a similar sort of balancing in the context of the Privileges and Immunities Clause. First, the Court determines whether a state regulation burdens a fundamental privilege of nonresidents.¹⁰⁴ If the regulation does burden a fundamental privilege, the Court will still uphold the discriminatory regulation if the state can demonstrate that nonresidents are a "peculiar source of evil" to residents and that the discrimination is substantially related to that evil.¹⁰⁵

The Supreme Court's decision in *United Building & Construction Trades Council v. Mayor of Camden*¹⁰⁶ applied this analysis to the city of Camden's preferential municipal ordinance, which required at least forty percent of the employees of contractors or subcontractors working on city construction projects to be Camden residents.¹⁰⁷ The Supreme Court determined that the opportunity to seek a job with these private employers is "sufficiently basic to the livelihood of the Nation" as to fall within the purview of the Privileges and Immunities Clause.¹⁰⁸ On the record presented, the

102. See *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204 (1983).

103. See *supra* notes 7, 26.

104. See *Baldwin v. Montana Game & Fish. Commn.*, 436 U.S. 371, 383 (1978); *Toomer v. Witsell*, 334 U.S. 385, 396 (1948). The concept of a "fundamental privilege" is more expansive than the concept of a "fundamental interest" under other provisions of the Constitution. The Equal Protection Clause, for example, defines fundamental interests to include only those rights explicitly or implicitly guaranteed by the Constitution, such as the right to vote, see *Harper v. Virginia Bd. of Elections*, 383 U.S. 663 (1966), or the right of interstate migration, see *Shapiro v. Thompson*, 394 U.S. 618 (1969). Fundamental privileges under the Privileges and Immunities Clause include many of the same interests, but they also include interests such as access to medical services, see *Doe v. Bolton*, 410 U.S. 179 (1973); equal taxes, see *Austin v. New Hampshire*, 420 U.S. 656, 661 (1975); private jobs, see *Hicklin v. Orbeck*, 437 U.S. 518 (1978); and "the pursuit of happiness," see *Paul v. Virginia*, 75 U.S. (8 Wall.) 168, 180 (1869).

105. *Baldwin*, 436 U.S. at 383; *Toomer*, 334 U.S. at 398.

106. 465 U.S. 208 (1984).

107. See 465 U.S. at 210. Camden enacted the ordinance pursuant to a statewide affirmative action program subject to the State Treasurer's approval. Because of this statewide program, the Court stated that the constitutional challenge to the preference law must also "be interpreted as a challenge to the State Treasurer's general power" to adopt such a preference." 465 U.S. at 215 (quoting *United Bldg. & Constr. Trades Council v. Mayor of Camden*, 443 A.2d 148, 154 (N.J. 1983)). Therefore, the Court's analysis arguably applies to state-mandated preference laws as well.

108. 465 U.S. at 221-22 (quoting *Baldwin v. Montana Fish & Game Commn.*, 436 U.S. 371, 388 (1978)). It is unclear whether, in the context of a state-mandated preference law, access to public construction jobs should constitute a fundamental privilege. The only court to address this issue implicitly held that access to such jobs should constitute a fundamental privilege. See *W.C.M. Window Co. v. Bernardi*, 730 F.2d 486, 497-98 (7th Cir. 1984). This result makes sense, especially when the resident construction workers are actually working for private contractors. Even when the construction workers work directly for the government, however, access to their jobs should probably constitute a fundamental privilege. Otherwise states could merely pay workers directly rather than through contractors and

Court would not decide whether economic and social problems in Camden justified the preference law.¹⁰⁹ The Court definitely implied, however, that some preference laws can survive scrutiny under the Privileges and Immunities Clause.¹¹⁰

The approach taken by lower courts applying the Privileges and Immunities Clause to resident-preference laws — and in one case a state-mandated preference law¹¹¹ — provides particularly apt guidance for analyzing such laws under the market-participant exception to the dormant Commerce Clause. First, these courts examine the record for evidence that nonresidents actually pose an economic “evil” to residents.¹¹² If the state cannot establish this threshold fact, then the court will automatically strike down the preference law.¹¹³ Next, these courts determine whether the state has narrowly tailored an appropriate remedy.¹¹⁴ The test requires a close fit between the evil posed by nonresidents and the remedy for that evil.¹¹⁵ When courts strike down resident-preference laws, generally the state has failed to produce evidence of an evil to be corrected or it has failed to narrowly tailor the remedy.¹¹⁶

As under the Privileges and Immunities Clause, courts should carefully scrutinize resident preference laws under the market-participant exception. First, they should ensure that the state has a legitimate basis for the preference — that the state is actually redistributing the residents’ money. Then they should demand evidence of a positive local benefit that the preference law will achieve beyond merely increasing the income of residents.¹¹⁷ For example, the preference law might aim temporarily to alleviate serious unem-

avoid the strictures of the Privileges and Immunities Clause. *But see* Massachusetts Bd. of Retirement v. Murgia, 427 U.S. 307, 313 (1976) (holding that there is no fundamental right to government employment for the purposes of the Equal Protection Clause).

109. The Court remanded the issue, but the case settled before the state court could make a final determination of whether sufficient reasons existed for the discrimination. *See* 1st Westco Corp. v. School District, 811 F. Supp. 204, 207 (E.D. Pa. 1993).

110. *See* Gergen, *supra* note 77, at 1100 n.12 (noting that “the Court [in *United Building*] clearly indicated that hiring preferences for citizens are sometimes permissible”).

111. *See* *W.C.M. Window*, 730 F.2d at 497-98 (striking down a state-mandated preference law because Illinois failed to produce evidence of the evil the state wanted to correct).

112. *See, e.g., W.C.M. Window*, 730 F.2d at 497-98; *1st Westco*, 811 F. Supp. at 207-08.

113. *See* *W.C.M. Window*, 730 F.2d at 497-98.

114. *See* *1st Westco*, 811 F. Supp. at 207-08.

115. *See* *TRIBE*, *supra* note 5, § 6-35, at 544 (comparing the Supreme Court’s “insistence on a fairly precise fit between remedy and classification” to the Warren Court’s strict scrutiny of Equal Protection and First Amendment issues).

116. *See* *W.C.M. Window*, 730 F.2d at 497-98; *1st Westco*, 811 F. Supp. at 207-08; *see also* *Neshaminy Constructors v. Krause*, 437 A.2d 733, 737 n.6 (N.J. Ch. 1981), *modified on unrelated grounds and aff’d*, 453 A.2d 1359 (N.J. App. 1982); *Salla v. County of Monroe*, 399 N.E.2d 909 (N.Y. 1979); *Laborers Local Union No. 374 v. Felton Constr.*, 654 P.2d 67 (Wash. 1982).

117. *Cf. Reeves, Inc. v. Stake*, 447 U.S. 429, 451 (1980) (Powell, J., dissenting) (arguing that the Court should first determine whether the state “participated in the market as a pri-

ployment in a particular geographic area or type of employment, such as highway construction, or it might temporarily buy the products of a struggling health-sensitive resident industry, such as milk production.¹¹⁸ Furthermore, courts should ensure that a resident preference law is reasonably necessary to achieve this benefit. In particular, courts should examine whether any less discriminatory alternatives exist,¹¹⁹ or whether the state has limited the temporal or economic scope of the regulation. For example, the state might supply some of the money to operate the preference law, or the law might only last for six months, or it might only apply to major urban areas or particular industries, or it might limit the percentage of purchases or job openings that will favor residents.¹²⁰ This analysis will ensure that states do not enact regulations that unduly burden interstate commerce. If the state fails to produce evidence of a sufficient local benefit or if the state fails to narrowly tailor its preference law, then a court should strike the law down as a violation of the dormant Commerce Clause. Otherwise, a court should uphold the law under the market-participant exception.

B. *Resolving the Split Between the Circuit Courts of Appeals*

An analysis of the opinions of those circuits that have passed on the constitutionality of state-mandated preference laws demonstrates the utility of applying the substantive approach outlined in this Note to such laws rather than the current market-participant approach. The substantive approach avoids the difficulty of attempting to determine whether a particular local government is dependent upon the state government or whether it in fact retains sufficient autonomy. Moreover, the substantive approach allows courts to distinguish between state-mandated preference laws that comport with the rationales for the market-participant exception and those that do not.

Applying the substantive market-participant exception approach suggests that the Seventh Circuit Court of Appeals correctly

vate firm" and then evaluate whether the state's action "burdens the flow of interstate commerce").

118. See *Dean Milk Co. v. Madison*, 340 U.S. 349 (1951) (recognizing that ensuring the supply of wholesome milk is a valid state objective).

119. See *supra* note 30 and accompanying text; see also *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204, 225 (1983) (Blackmun, J., concurring in part and dissenting in part) (arguing that Boston could have devised less discriminatory alternatives to its resident preference law).

120. But see *White*, 460 U.S. at 217 n.3 (Blackmun, J., concurring in part and dissenting in part) ("That the order limits the preference to 50% of the covered jobs is, of course, not relevant to the applicability of the market participant exemption. If such preferences do not implicate the dormant Commerce Clause, they are immune even if they apply to 100% of a contractor's jobs.").

decided *W.C.M. Window Co. v. Bernardi*.¹²¹ In this case, the Seventh Circuit struck down a state-mandated preference law requiring *all* contractors with local governments to hire *only* Illinois residents unless such residents were unavailable.¹²² The court noted that Illinois failed to produce any evidence on the employment rate in Illinois's construction industry, the costs to the state of unemployment, the effect of a resident preference on unemployment, or the benefit of the preference compared to the inefficiency of not hiring nonresidents.¹²³ In addition, the court relied on an uncontradicted affidavit that the state did not even partially finance the operation of the law as it applied in the case.¹²⁴ Thus, Illinois failed to adduce any evidence of the benefit of the state-mandated preference law, and it failed to narrowly tailor the law by supplying some money to the local governments or limiting the number of contractors to whom the law applied. Although Illinois may legitimately spend its own money to benefit residents in some instances, the State failed to prove that the benefit of this regulation exceeded its burden on interstate commerce.

The substantive approach to applying the market-participant exception also suggests that the Third Circuit Court of Appeals correctly decided *Trojan Technologies v. Pennsylvania*.¹²⁵ In this case, the Third Circuit upheld a law that required all local governments to buy American-made steel.¹²⁶ The court's focus on the relationship between the state and its local governments,¹²⁷ however, demonstrates how that approach ignores the real concerns of the dormant Commerce Clause. The real dormant Commerce Clause concern implicated in *Trojan Technologies* was the burden on interstate commerce created by the buy-American law. Proper analysis of this issue would begin by noting that a buy-American law does not discriminate against other states; it merely discriminates against foreign commerce. Such a law does not pose a threat to *interstate* commerce. Courts examining state-mandated buy-American laws must ensure only that such laws do not unduly burden *foreign* commerce.¹²⁸ If a state-mandated buy-American law does not unduly burden foreign commerce, then a court should *always* uphold the

121. 730 F.2d 486 (7th Cir. 1984).

122. See *supra* note 14.

123. See *W.C.M. Window*, 730 F.2d at 498.

124. See 730 F.2d at 495.

125. 916 F.2d 903 (3d Cir. 1990).

126. See 916 F.2d at 904-05.

127. See 916 F.2d at 910-12.

128. See 916 F.2d at 912-13; see also *Reeves, Inc. v. Stake*, 447 U.S. 429, 437-38 n.9 (noting in a market-participant case that Commerce Clause scrutiny may be higher when foreign commerce is involved).

law under the market-participant exception to the dormant Commerce Clause.

In *Big Country Foods v. Board of Education*,¹²⁹ the court's decision seems inconsistent with a more substantive approach to the market-participant exception. The Ninth Circuit upheld an Alaskan preference statute that required schools receiving funds from the state government to buy dairy products harvested in the state, despite the fact that the federal government in fact supplied the funds for the program.¹³⁰ Because Alaska did not actually supply the funds, it did not have a legitimate entitlement to prefer its own citizens.¹³¹ Nevertheless, the case provides a good example of how a state can diminish the effect on interstate commerce of a state-mandated preference law. The state limited the program to a single group of local government entities — school boards — and to a single type of product — milk. Moreover, the state required the school boards to buy like-quality, nonresident-harvested milk when the price of resident-harvested milk exceeded nonresident prices by more than seven percent.¹³²

CONCLUSION

Courts should take a more substantive approach to applying the market-participant exception to state-mandated preference laws rather than focusing on state-local government relationships. This substantive approach should recognize the concerns of the dormant Commerce Clause — allowing legitimate state regulation while preventing undue burdens on interstate commerce — and the legitimate justifications for the market-participant exception — preferring residents with state funds in a manner that poses less risk of burdening interstate commerce. First, the court should ensure that the preference law applies to the expenditure of state or local resident funds, rather than federal or nonresident funds. Then, it

129. 952 F.2d 1173 (9th Cir. 1992).

130. See 952 F.2d at 1175, 1179-80.

131. The court expressly rejected this argument under its interpretation of *White v. Massachusetts Council of Constr. Employers*, 460 U.S. 204 (1983). See *Big Country*, 952 F.2d at 1179-80; see also *Swin Resource Sys. v. Lycoming County*, 883 F.2d 245, 250 (3d Cir. 1989), cert. denied, 493 U.S. 1077 (1990) (rejecting, on the basis of *White*, the argument that federal funding made the market-participant exception inapplicable). The court in *Big Country* stated at great length, however, its apparent sympathy with the argument that the use of federal funding should make a difference:

We recognize there are strong public policy arguments to the contrary. It may be asserted with some logic that the use of federal as opposed to state or local funding allows Alaska to reap what it has not sown; that the underlying commerce clause value of a free market is undermined when the federal government in essence subsidizes one state's industry; and that a state differs from the usual market participant in that the state has the ability to obtain federal subsidies for its purchases.

952 F.2d at 1180 (citation omitted).

132. See 952 F.2d at 1175.

should examine whether the preference's burden on interstate commerce substantially outweighs the state's proffered benefit. If the state cannot provide adequate evidence of the benefit, if less discriminatory alternatives exist, or if the burden of the preference law is too great, then the court should strike down the law as a violation of the dormant Commerce Clause. Otherwise, the court should uphold the law under the market-participant exception.

Ultimately, courts should apply this more substantive market-participant exception to all resident-preference laws. The Supreme Court's current market-participant jurisprudence implies that whenever a state is directly participating in the market by spending its own funds, the Court will uphold a discriminatory resident preference without examining its burden on interstate commerce. The limitation posed by the dormant Commerce Clause on the rationales for the market-participant exception is the same, however, whether a preference law operates only on the state government or whether it operates on local governments as well — at some point even the most justifiable resident preferences can impose an unreasonably high burden on interstate commerce. Adopting the substantive approach to the market-participant exception for all resident-preference laws would bring logic and consistency into this area of the law by providing clear guidelines for lower courts and by harmonizing market-participant doctrine with existing dormant Commerce Clause and Privileges and Immunities jurisprudence.